

**DEPARTMENT OF STATE REVENUE**

**LETTER OF FINDINGS NUMBER: 04-0124**

**Corporate Income Tax  
For Tax Years 1996 and 2000**

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

**I. Corporate Income Tax—Consolidated Return**

**Authority:** IC 6-8.1-5-1(b); 45 IAC 15-5-3(b); IC 6-3-4-14; IC 6-3-2-2(l)

Taxpayer protests that it should be included in the Indiana consolidated return.

**II. Tax Administration—Negligence Penalty and Interest**

**Authority:** IC 6-8.1-10-2.1; 45 IAC 15-11-2; IC 6-8.1-10-1(e)

Taxpayer protests the imposition of a ten percent negligence penalty and interest.

**STATEMENT OF FACTS**

Taxpayer is a Delaware corporation that is headquartered in California. More facts will be provided as needed below.

**I. Corporate Income Tax—Consolidated Return**

**DISCUSSION**

Before examining the taxpayer's protest, it should be noted that the *taxpayer* bears the burden of proof. IC 6-8.1-5-1(b) states in pertinent part:

The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made.

The Indiana Administrative Code also states "[t]he burden of proving that a proposed assessment is incorrect rests with the taxpayer...." 45 IAC 15-5-3(b).

The auditor stated the following regarding the taxpayer:

[The taxpayer's] function is to provide management services that includes, to supervise and maintain business operations at [Company X] and to promote sales. Management fees were paid to [taxpayer] only in 1996 and 1997.... In 1998 and 2000 [taxpayer's] only income was from a nominal amount of interest income. [Taxpayer] does not have nexus in Indiana nor does it have any income from Indiana sources. The management services, when performed, were performed in California. Its income, losses, apportionment factors are being deleted from the tax returns.

Regarding the taxpayer's argument, it should be noted that taxpayer's initial protest letter and its subsequent protest letter offer what appear to be different arguments (the former unitary, the subsequent consolidated). The taxpayer in the subsequent letter (dated February 23, 2006) states:

Taxpayer intends that this [2/23/06 letter] Amended Protest and Request for Hearing relate back to the Original Protest and amend same to set forth the following grounds for relief which shall *supersede and strike the Grounds for Taxpayer's Disagreement found in its Original Protest....*

(*Emphasis added*). Thus the arguments from the "Original Protest" letter are not addressed in this Letter of Finding, since the taxpayer in effect told the Department to disregard the initial ("Original Protest") letter.

IC 6-3-4-14 provides that, "An affiliated group of corporations shall have the privilege of making a consolidated return with respect to the taxes imposed by IC 6-3." Thus the taxpayer argues that it "should be included in the consolidated Indiana Return for the Audit Period." Taxpayer states the following:

[Taxpayer] ("Designated Agent") was a Delaware corporation with its commercial domicile located in Yorba Linda, California. During the Years-at-Issue, Designated Agent was engaged in several business activities within the state of Indiana, including, but not limited to; receipt of management fees from management services it performed for [Company X], its subsidiary, located in Indiana; employment of one employee at [Company X]; reimbursement of travel expenses for multiple officers who met, on several occasions, at the [Company X] facility; the Guarantee and payment of rent obligations on behalf of [Company X] for third-party asset lease obligations in Indiana; payment of royalty expenses on behalf of [Company X] for third-party royalty agreements in Indiana; payment on behalf of [Company X] for certain 1997 real estate and personal property taxes located in Indiana; payment of employee life insurance premiums on behalf of the [Company X] facility in Indiana; and receipt of interest income from loans to [Company X] where the proceeds of such loans were applied in Indiana for the above-mentioned expenses.

Despite taxpayer's above assertions regarding property, payroll, and sales, the audit report does not appear to show any Indiana property, payroll, or sales for the taxpayer. For example, the

taxpayer claims to have an Indiana employee, but no Indiana payroll is shown in the audit; the taxpayer claims to have interest from Indiana but no Indiana receipts are reflected in the audit. Taxpayer had no Indiana source income, since there were no Indiana numerators in the taxpayer's apportionment.

Additionally, even if the taxpayer were to prevail, *arguendo*, on its argument regarding nexus the taxpayer still loses on other grounds. Namely, IC 6-3-2-2(l), which states:

If the allocation and apportionment provisions of this article do not *fairly represent* the taxpayer's income derived from sources within the state of Indiana, the taxpayer may petition for or the department may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

- (1) separate accounting;
- (2) the exclusion of any one (1) or more of the factors;
- (3) the inclusion of one (1) or more additional factors which will fairly represent the taxpayer's income derived from sources within the state of Indiana; or
- (4) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

(*Emphasis added*). Since there appears to be no reported property, payroll, or sales, bringing substantial losses into Indiana runs afoul of the "fairly represent" language of IC 6-3-2-2(l).

### **FINDING**

Taxpayer's protest is denied.

## **II. Tax Administration—Negligence Penalty and Interest**

### **DISCUSSION**

Taxpayer protests the imposition of a ten percent penalty. The Department refers to IC 6-8.1-10-2.1 and to 45 IAC 15-11-2(b), the latter of which states:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

45 IAC 15-11-2(c) provides in pertinent part:

The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section.

The taxpayer argues its “conduct was based on a bona fide question of law with respect to its activities and was not due to negligence or willful neglect.” However, as noted in Section I, *supra*, the taxpayer bears the burden of proof. The taxpayer has failed to adequately develop its argument and meet that burden of proof. (It should also be noted that the taxpayer did not develop any argument regarding interest, and the Department refers to IC 6-8.1-10-1(e)).

### **FINDING**

Taxpayer’s protest is denied.

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